



Pension Benefit Guaranty Corporation
1200 K Street, N.W., Washington, D.C. 20005-4026

FOIA 2005-0987

July 22, 2005

The Honorable George Miller
Senior Democratic Member
Committee on Education and the Workforce
U.S. House of Representatives
2181 Rayburn House Office Building
Washington, D.C. 20515-6100

Re: Pension Reform Proposal

Dear Congressman Miller:

This is in response to your Freedom of Information Act (FOIA) request dated June 22, 2005. Pursuant to your request, a search of agency records has been conducted and I am providing information that appears to fall within the scope of your request. The following represents an item-by-item response to your request:

Under item number one, you have requested "In dollar amounts, the aggregate amount of additional (and total) pension contributions that will be required under the Administration's proposal compared with current law, and current law with the corporate bond rate, by year, from 2005 through 2016." While we do not have the specific information you have requested, I have enclosed information that relates to your request. This material is marked as Enclosure 1.

Item two requests "The anticipated annual operating deficit/surplus of the PBGC for years 2005 through 2016 under the Administration's proposal versus current law." I have material marked as Enclosure 2 that provides responsive information.

With respect to item three, our search has failed to locate any records containing hypothetical examples of how companies would be affected by the Administration's proposal.

Under item number four, you request "An estimate of when PBGC will run out of cash to pay claims under current law versus the Administration's plan." Our search has failed to locate any document containing this information.

Item number five requests the number of financially weak companies as determined under the Administration's proposal. A search of agency records has failed to locate any records containing this information.

Under item number six, you have requested "The savings to the PBGC associated with the Administration's plan to perfect liens in bankruptcy". Our search of agency records failed to uncover the analysis requested. However, on June 30, 2005, our Executive Director provided a response to your previous inquiries that included the following example of such savings:

"For example, if PBGC had the ability to perfect liens in bankruptcy, liens totaling \$770 million could have (and most likely would have) been perfected against United Airlines. The actual recovery would have depended on the unencumbered assets subject to the lien."

Under item seven, you have requested the savings to the PBGC associated with the Administration's plan to limit contingent liability benefits. In the June 30 letter referenced above this question is addressed as follows:

"We estimate that the value of unfunded shutdown benefits in DB plans today exceeds \$10 billion. Unless the law is changed, the PBGC will most likely assume a sizable portion of that amount."

In item eight, you have requested the average and median increase (for underfunded plans) in contributions and premiums for companies by year from 2005 through 2016 for current law versus Administration's proposal. Our search has failed to uncover the analysis requested. However, with regard to contributions, our June 30 letter referenced above provided the following example:

"For example, for the first ten years the proposal is in effect, required contributions will increase approximately 29% under the stable economy scenario described in the Funding Reform White Paper. If the projection period were expanded to 20 or 30 years, the average increase, if any, would be significantly lower, because, as explained above, the ultimate cost of providing benefits does not change."

With respect to item nine, you have requested a distributional analysis of how many plans would have to increase contributions and by how much. Our search has failed to uncover any records that contain the requested analysis.

Under item number ten, you have requested "An analysis on the number of plans that are expected to freeze or terminate as a result of the Administration's proposal over the next ten years." Our search has failed to locate the requested analysis. As noted in the June 30, 2005, letter:

"The variables contributing to a company's decision to freeze or terminate a pension plan are numerous, and largely unique to its own financial and human resource needs."

You asked that e-mail be searched for any relevant records. I have not completed the search of all e-mail that may be encompassed by this request. I estimate that in excess of 100,000 e-mail messages may need to be reviewed to determine if any fall within the scope of your request. Based on our review thus far, it appears that e-mails are pre-decisional and not appropriate to disclose under the FOIA.

Sincerely,

A handwritten signature in black ink, appearing to read "E. William FitzGerald", written over a horizontal line.

E. William FitzGerald
Disclosure Officer

Enclosures

Enclosure 1

Future contribution requirements are dependent on several factors. These include:

- Future financial market events including changes to the interest rates used to value pension liabilities and the returns on pension assets.
- Decisions by plan sponsors on plan funding (whether or not to contribute above minimum requirements, and by how much), benefit increases, how to invest plan assets, whether or not to freeze plans, whether to convert other types of plans to cash balance, the setting of actuarial assumptions, etc.
- Future expansion or contraction of different industries and/or specific companies sponsoring defined benefit pensions.
- Pension funding rules.

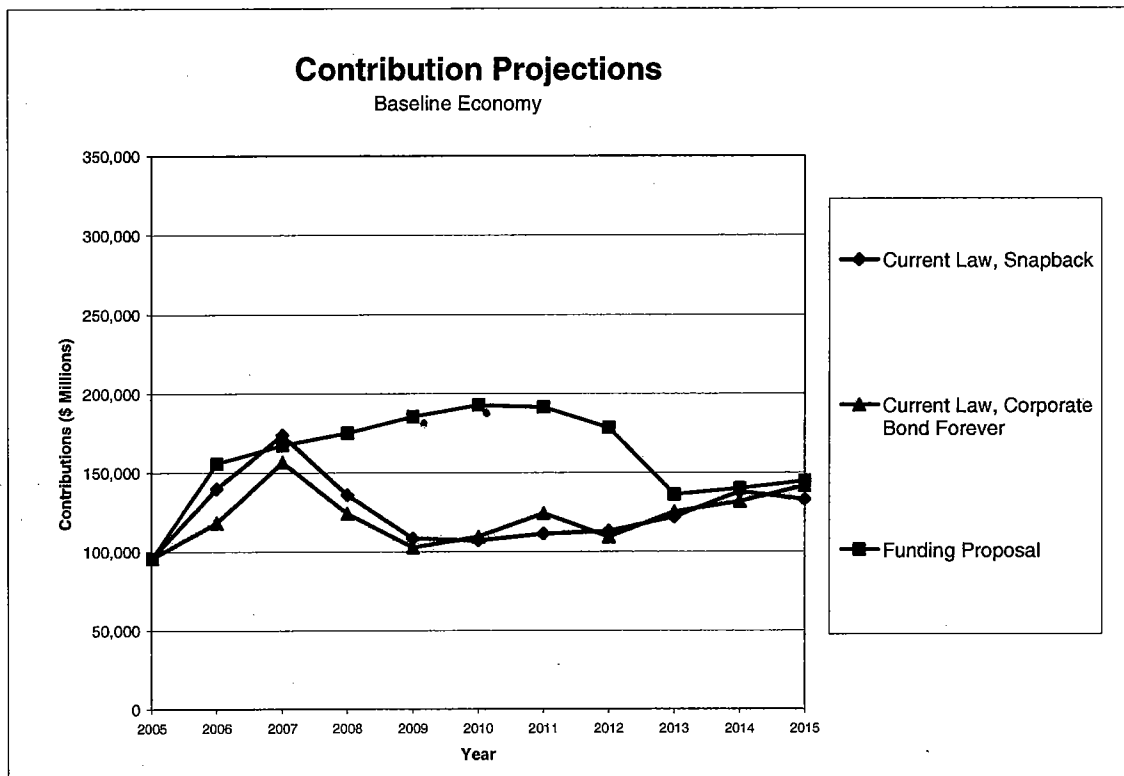
PBGC's projections of future pension funding examine the effects of changes to elements of the last of those factors, the pension funding rules. Since the futures of the other factors are unknowable, it is impossible to state with exactness what future funding requirements will be. Instead, PBGC simulates future contributions under various combinations of potential futures for other factors.

The following projections are based on PBGC's baseline assumptions. This baseline assumes stability of interest rates and asset returns, plan sponsor choices, and sponsor composition. It also assumes that sponsors contributions to plans are the lowest allowable by the funding rules. Since such extreme stability is unlikely to actually unfold, the following results are not directly comparable to results that might be generated by analyzing the proposal's effects under any specific forecast of future economic conditions or path of defined benefit pension plan participation.

These results do not reflect the effects of some critical components of the proposal including the direct and incentive effects of benefit restrictions and the incentive effects of the proposed system of PBGC premiums. The proposal provides plan sponsors with both the tools and incentives to smooth contributions by funding above the minimum during good times. Projected minimum contributions do not reflect this behavior — that is, sponsors are not assumed to take advantage of new rules that allow sponsors to build funding cushions in good economic times. PBGC's white paper does discuss a stylized example of how a representative sponsor might use these rules to make the path of required contributions less volatile over time.

As shown below, under the baseline assumption scenario, contributions increase during the first several years under the Administration's Funding Proposal,

Current Law, and Current Law using Corporate Bond Rates in the DRC rules. Contributions under both Current Laws then drop due to a major flaw in current law—plans are not required to be fully funded. This of course results in losses to both workers and the insurance program.



This graph of this scenario paints an incomplete picture since it does not also show the resulting plan funded ratios and claims to workers and the insurance. Further, this contribution pattern is illustrative of just one scenario about the future—they are not a prediction or best estimate of future results.

Modeling Notes

This analysis was performed using the PBGC's Pension Insurance Modeling System (PIMS). PIMS has a detailed database of about 400 actual plans, sponsored by nearly 300 firms, which represent about 50 percent of liabilities and underfunding in the defined benefit system. The database includes the plan demographics, plan benefit structure, asset values by type, liabilities, and actuarial assumptions. It also includes key financial information about the employer sponsoring the plan.

PIMS simulates contributions and underfunding for these plans using the minimum funding rules under the Administration's proposal and current law,

and then extrapolates the results to the universe of single-employer plans. It also uses the employer financial information as the starting point for assigning probabilities of bankruptcy, from which it projects losses to the insurance program under both current law and the funding proposal.

The PIMS model is not predictive. That is, it is not intended to provide a single best estimate of future events. It is most useful in demonstrating the relative affect of different policy proposals, rather than identifying specific outcomes. When used in a stochastic mode, PIMS provides a range of possible outcomes under 500 different economic scenarios.

The PIMS results do not take into account possible incentive effects from the Administration's proposal. For example, it does not take into account the possibility that plan sponsors will take advantage of the increased "cushions" that will allow them to make larger tax-deductible contributions in good years, or the possibility that they will make additional contributions to reduce their PBGC premiums. The model also does not incorporate behavioral responses to economic conditions, such as the possibility that companies in a single industry will seek to terminate their plans in response to the termination of their competitors' plans.

The PIMS results shown above and in the PBGC's White Paper will be updated in the near future to reflect new information (e.g., the contributions for 2003 plan years that have recently become available).

Baseline Assumptions

- Interest rates and equity returns were set (approximately) to the medians of their historical values. Those rates, and other key parameters, were set as follows:
 - 30-year Treasury yield 5.0%
 - Equity return 9.0%
 - Plans' return on assets 6.9%
 - Inflation 2.5%
 - Wage and benefit growth 4.2%
- Sponsor financial-health variables were fixed at their initial values.
- Plan asset allocations were fixed at mean values for all plans.
- Plan demographics. The number of active participants was fixed at the initial value, but age and service varied depending on retirement and hiring assumptions. The number, age, and benefits of retired and terminated vested participants varied depending on mortality, separation and retirement assumptions.

Below is a spreadsheet providing the single-employer net position for FY 2005-2016 under current law and under the Administration's proposal as included in PBGC's FY 2006 President's Budget Submission. Under the Administration's proposal, this deterministic projection assumed 1) strengthening of minimum funding provisions, 2) a flat premium set at \$30 per participant for 2006 plan years and increasing for assumed wage inflation thereafter, and a risk-based premium set by PBGC's Board at a level sufficient to eliminate the single employer deficit by the end of FY 2016.

PBGC SINGLE EMPLOYER PROGRAM NET POSITION 2005-2016--FY 2006 PRESIDENT'S BUDGET SUBMISSION												
\$ in billions	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Current Law	\$(27.347)	\$(29.656)	\$(31.995)	\$(33.838)	\$(35.452)	\$(36.945)	\$(38.462)	\$(39.921)	\$(41.430)	\$(42.871)	\$(44.289)	\$(45.890)
Administration's Proposal	\$(27.347)	\$(27.451)	\$(25.894)	\$(23.857)	\$(21.381)	\$(18.720)	\$(16.045)	\$(13.176)	\$(10.142)	\$(7.036)	\$(3.586)	\$ -
The Administration's proposal included in the FY 2006 budget assumed elimination of PBGC's single employer deficit by the end of FY 2016												